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Greater Price Uncertainty and Its Effects

A sharp fall in the price of oil will greatly increase uncertainty about the future oil price. In the past several years there has been a consensus in the market that the real price of oil would vary gradually, perhaps slowly upward, perhaps downward.

With a plunge in 1983, market expectations are likely to encompass a further sharp decline in price to a rebound -- sooner or later -- to a higher level.

This uncertainty will create more perceived risk in the marketplace. It will affect exploration and production decisions of oil companies and the investment decisions of oil-using consumers. Many firms and individuals may respond by deferring major oil-related investments until price uncertainty reduces. This price uncertainty will also be used as an argument for governments of oil-importing countries to act to stabilize the internal price of oil.